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FIDUCIARY PROVISIONS OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974

*John J. Weiler**

INTRODUCTION

The Employee Retirement Income Security Act of 1974 (ERISA)¹ is an extremely complex and massive piece of legislation whose full impact has yet to be realized. Its complexity is attributable in no small part to the dual jurisdiction allocated between the Labor Department and the Treasury Department and its many substantive and procedural provisions. Its mass is attributable to its breadth of coverage, from a small, fully-insured medical hospitalization plan to a complicated, union-negotiated pension plan. Literally, upon establishing any employee fringe benefit plan, ERISA applies from inception to termination.

The fiduciary provisions of ERISA are among the most complicated portions of the Act. These provisions range from abstract skeletal principles that necessitate future regulations and court interpretations to specific rules of prohibited and mandatory conduct. Most fiduciary provisions are not clearly illuminated or organized in the legislation but must be extracted by cutting and pasting; their full import and impact will only be realized with the passage of time.

LEGISLATIVE HISTORY OF THE FIDUCIARY PROVISIONS

The private pension system is of relatively recent origin in the United States. It is in large part attributable to the change in our society from a rural agrarian to a highly industrialized urban one. In an industrial society, the laborer sells his services in return for wages, and when he is no longer able to sell those services he is forced to live off the wages previously earned and saved. It was thus only natural for laborers to be concerned with deferring some of their current

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1. P.L. 93-406 (September 2, 1974) [hereinafter cited as ERISA]. For a complete legislative history, see CONGRESSIONAL RESEARCH SERVICE, LIBRARY OF CONGRESS, HD 7100, 74-183 Ed. (1974).

wages to their retirement years. The inability of a substantial portion of the American workers to provide for their own retirement through savings and the inadequacy of the amounts saved and the consequences flowing from this result was one of the prime reasons for the federal government's injecting itself into the retirement picture. In 1935, Congress enacted the Federal Old Age, Survivors and Disability Insurance Program, which has been expanded both in coverage and in benefits in subsequent years.² Though the federal government had entered into the retirement picture through the enactment of a federal retirement system,³ it had, before the enactment of ERISA, exercised relatively little control over private pension systems.

The growth in private pension plans in the United States has been tremendous. In 1950, it was estimated that 9.8 million workers were covered by some form of private pension plan.⁴ In 1960, the figure had increased to over 21 million, and by 1969, over 29 million workers were covered.⁵ It was estimated that in 1974 over 30 million workers, almost one-half of the private non-farm working force, were covered by some form of private pension plan.⁶ The phenomenal rate of expansion in coverage was also matched by the accumulation of pension assets. In 1974, it was estimated that assets in excess of 372 billion dollars were held as reserve in various pension plans.⁷ These assets constituted the largest unregulated source of capital in the United States. In view of these factors, it was only a matter of time before encompassing federal regulatory legislation was enacted in the private pension area.

On March 28, 1962, President John F. Kennedy established a blue-ribbon federal cabinet-level committee to review

2. 49 Stat. 620; 42 U.S.C. § 301 (1970).

3. *Id.*

4. INTERIM REPORT OF ACTIVITIES OF THE PRIVATE WELFARE AND PENSION PLAN STUDY, SUBCOMMITTEE ON LABOR, REPORT OF THE COMMITTEE ON LABOR AND PUBLIC WELFARE, S. REP. NO. 92634, 92d Cong., 2d Sess. 11, Table 7 (1972).

5. *Id.*

6. H. REP. NO. 93-533, 93d Cong., 2d Sess. 259 (1974).

7. 34 SEC STATISTICAL BULLETIN no. 12 (Dec. 1975). Included in this figure are the assets of private pension plans, state and local government retirement funds, and pension funds administered by the federal government. Total assets of private noninsured pension funds at the end of 1974 were \$133.7 billion (book value).

"the implications of the growing retirement and welfare funds for the financial structure of the economy, as well as . . . review . . . the role and character of the private pension and other retirement systems in the economic security of the nation, and . . . [consider] . . . how they may contribute more effectively to efficient manpower utilization and mobility."⁸ In January, 1965, the committee presented its massive report to President Lyndon B. Johnson.⁹ The legislative recommendations of the committee were the foundation for substantive provisions of ERISA. In fact, the major recommendations of the committee, except for portability of pension benefits, were enacted into law through ERISA, with some modifications.¹⁰

The Cabinet committee found that private retirement plans had a major impact on the nation's economy and tax base, and found major areas of deficiency in the private pension system.¹¹ In turning to the fiduciary area, the committee indicated that the real problem was not the lack of an appropriate fiduciary standard but rather the enforcement of that standard by and in behalf of participants and the disclosure to those participants of their rights and benefits.¹² The committee found that generally, the standard of fiduciary conduct established by custom and law in the private trust area was adequate and adaptable to the private pension area. It did

8. Memorandum from President John F. Kennedy to the Secretary of Labor, Secretary of the Treasury, the Secretary of Health, Education and Welfare, the Director of the Bureau of the Budget, the Chairman of the Council of Economic Advisors, the Chairman of the Board of Governors of the Federal Reserve System, and the Chairman of the Securities and Exchange Commission, titled *In Re the Establishment of a Committee on Corporate Pension Funds and Other Private Retirement and Welfare Programs*, March 28, 1962.

9. PUBLIC POLICY AND PRIVATE PENSION PROGRAMS, A REPORT TO THE PRESIDENT ON PRIVATE EMPLOYEE RETIREMENT PLANS BY PRESIDENT'S COMMITTEE ON CORPORATE PENSION FUNDS AND OTHER PRIVATE RETIREMENT AND WELFARE PROGRAMS (Jan. 1965).

10. *Id.* at ix, xi-xii.

11. *Id.* at xv. The committee indicated that \$6 billion are contributed annually to qualified pension plans, and since these amounts are deducted by the employer on his tax return and not taxed as current compensation to plan participants, the government is in fact subsidizing private pension plans. A Qualified Pension Trust is not a taxable entity and thus earnings accumulate tax free, which is a loss of revenue for the federal government.

12. *Id.* at 73. The committee felt that the general standard of fiduciary conduct in the private trust area, with its long and established history, was well suited and viable for the pension area.

recognize that certain accepted and widely used practices that did not necessarily violate traditional trust law were not in the best interest of plan participants and should be prohibited.

The Cabinet committee found a deficiency in disclosure to plan participants of their rights and benefits and the establishing of effective measures for the enforcement of plan participants' rights. In reviewing existing legislation, the committee came to the conclusion that it was deficient in this regard and specifically recommended that the Welfare and Pension Plan Disclosure Act be amended in order to require fuller disclosure to plan participants.¹³

Though the Cabinet committee found a deficiency in existing disclosure requirements it concluded that disclosure to plan participants in and of itself is not sufficient unless effective means are established to protect the rights of plan participants and provide methods for enforcing them. It also indicated that it may be necessary to designate or create a federal regulatory agency as guardian for the collective interest of plan participants and their beneficiaries and to empower that agency with the necessary authority to bring court proceedings to enforce those rights.¹⁴

Most of the committee recommendations lay relatively dormant until March 1, 1971, when the United States Senate passed a resolution directing the Subcommittee on Labor of the Committee on Labor and Public Welfare to "conduct a general study of pension and welfare funds with special emphasis on the need for protection of employees' coverage."¹⁵ The Subcommittee thoroughly investigated the private pension field and wrote a lengthy Committee Report concluding with certain recommendations and legislative proposals.¹⁶

13. *Id.* at 78. The committee recommended amending the Welfare and Pension Plans Disclosure Act to require disclosure of additional information similar to what is required of investment companies under S.E.C. regulations.

14. *Id.* at 77. The committee pointed out that full disclosure of all relevant facts to plan participants is a prerequisite to self-help. It is obviously impossible for plan participants to enforce their rights unless they are aware that their rights have been violated.

15. S. Res. 35, § 4, 92d Cong., 1st Sess., 117 CONG. REC. Part 37 at 1681. This resolution in fact continued prior S. Res. 360, 91st Cong., 2d Sess., 116 CONG. REC. Part 34 at 1315.

16. The Subcommittee on Labor, pursuant to the mandate of the Senate Resolution, undertook as part of its comprehensive study a survey and analysis of approximately 1500 private plans selected on the basis of a statis-

Testimony by plan participants at legislative hearings convinced members of the Subcommittee of the need for legislation in basically the same areas that had been found deficient by the blue-ribbon Cabinet committee some six years previous, namely, vesting,¹⁷ portability,¹⁸ funding,¹⁹ reinsurance²⁰ and fiduciary standards. Plan participants indicated that they sustained irreparable financial hardship at the time of their termination of employment or retirement, realizing too late that pension benefits on which they had relied did not exist. Responsive testimony by plan administrators and employers confirmed to a large degree the deficiencies, inadequacies and inequities described by employee-participants in previous hearings.²¹ The Subcommittee found that some employers welcomed and suggested federal legislation in

tically-designed sampling technique from 3400 plans on file with the U. S. Department of Labor. From the plans in the survey, two preliminary staff analyses were conducted. The first, released on March 31, 1971, concerned itself with the benefits and forfeitures in 87 of those private pension plans. The analysis demonstrated that the number of employees in the 87 plans who did not receive benefits or vested rights since 1950 greatly exceeded those who did receive benefits or vested rights. The second staff analysis, released on November 7, 1971, concerned itself with the amount of pension and retirement benefits received in 764 plans during 1969-70—an average of less than \$100 a month. SENATE SUBCOMM. ON LABOR OF THE COMM. ON LABOR AND PUBLIC WELFARE, PRELIMINARY REPORT ON THE PRIVATE WELFARE AND PENSION PLAN STUDY, S. Rep. 92-634, 92d Cong., 1st Sess. appendix (1971) [hereinafter cited as PRELIMINARY REPORT].

17. Of the 21 witnesses testifying at the July 27, 28 and 29, 1971, hearings, all of which were plan participants, 11 described forfeitures of pension benefits which were directly attributable to inequitable vesting standards or the lack of such in plans. *Id.* at 68. For a complete study of the vesting provisions in effect in existing plans as found by the Subcommittee, see *id.* at 119.

18. The Subcommittee realized that the question on portability was complex and would necessitate further government controls. It indicated that it was aware of the problem and like the President's Cabinet Committee Report discussed various alternatives but reaching no conclusions, recommended further study. *Id.* at 73.

19. The Subcommittee unequivocally stated that "insufficient funding of assets in pension plans presents an issue which warrants corrective legislative action." *Id.* at 72.

20. The establishment of the Pension Benefit Guaranty Corporation in ERISA was of course an outgrowth from the reinsurance discussions and thinking of the Committee. *Id.* at 74, 81.

21. On October 12 and 13, 1971, the Subcommittee invited a select group of employers and administrators to comment upon specific allegations and testimony received in the July hearings. Sixteen witnesses testified at the October hearing.

order to achieve corrections. The testimony also established that various investment practices, while not necessarily violating existing laws and though performed and undertaken with the best of intentions, nevertheless did present certain conflict of interest problems. For example, the Subcommittee found that investment of substantial plan assets in employer real estate or employer securities was a widespread practice.²²

The Senate Subcommittee concluded, as had the blue-ribbon Cabinet committee, that there was no single centralized governmental agency or regulatory body with supervisory authority over private pension plans. Though eleven federal departments and agencies had some authority and responsibility in the pension area, it was apparent that only two played a major role.²³

The Subcommittee recommended federal legislation requiring improved disclosure and communication of plan provisions to plan participants to be accomplished in part by strengthening the disclosure requirements in existing legislation.²⁴ It recommended a uniform standard of fiduciary responsibility and the centralization in one agency of all existing as well as prospective regulation of private pension plans, to the maximum extent feasible.²⁵

22. Though the Committee indicated that these practices do not necessarily violate existing federal or state legislation and even though they are performed with the best interests, nonetheless their potential can actually jeopardize plan assets and may not serve the best interests of the plan participants. PRELIMINARY REPORT at 86.

23. See *id.* at 91-99. The Committee sets forth an extensive discussion as to the extent of supervisory regulation exercised by the federal government over the administration and operations of private pension plans. The most direct supervision was exercised by the Department of Labor through its statutory requirements of plan disclosure and enforcement of certain federal criminal statutes. The Treasury Department, which through the Internal Revenue Service, is empowered to grant qualified status to pension plans and thus guarantee certain tax advantages, played a minor role in the regulatory process. See Lamon, *Fiduciary Standards Under the Employee Retirement Income Security Act of 1974*, LAW NOTES, BARRISTER (Summer 1975).

24. Both the July and October hearings established that a frequent problem experienced by worker-participants is that they are furnished very little information as to the administration and operation of their plan. The Subcommittee found that workers are not adequately advised on conditions governing their eligibility for plan participation nor are they adequately advised as to how pension benefits are and can be lost. PRELIMINARY REPORT at 112.

25. The Subcommittee specifically recommended "[a] uniform federal

TYPE OF PLANS WITHIN THE SCOPE OF ERISA

A plan fiduciary of a plan subject to ERISA bears the responsibility and potential liability imposed by the Act.²⁶ While ERISA contains four titles, the fiduciary provisions are found mainly in Title I.²⁷ Since its coverage is all-inclusive, its provisions are most important for present purposes.

Title I applies to all "employee benefit plans," defined as "employee welfare benefit plans," and "employee pension benefit plans," or a combination of both.²⁸ An "employee welfare benefit plan" is any plan, fund or program providing certain employee fringe benefits, such as medical, surgical, hospital care, accident, disability, death, unemployment, vacation benefits, apprenticeship or other training programs, day care centers, scholarship funds, or prepaid legal services.²⁹ The coverage is of such breadth that many employers may fail to realize that their fringe benefit plans fall within the definition of an employee welfare plan.

An "employee pension benefit plan" is a fund, plan, or program maintained by an employer or employee organization for the purpose of providing retirement income to employees or resulting in a deferral of income by employees

standard of fiduciary responsibility." *Id.* at 113. The Subcommittee indicated that it faced two competing schools of thought: one advocated stringent governmental controls, while the other, equally adamant in its position, resisted any further regulation contending that plan flexibility would be impeded. It stated that plan participants must have the assurance that pension benefits they have earned and come to rely upon will be available to them in their retirement years. Similarly, it realized that employers need flexibility in order to establish a pension program within the confines of their unique and individual structures.

26. Of course, the Act imposes responsibility and potential liability upon persons other than "fiduciaries," but the Act is only applicable to an employee organization engaged in or affecting commerce maintaining an "Employee Benefit Plan." ERISA §§ 4(a), 3(3).

27. Title I contains the labor provisions of ERISA while Title II contains the Internal Revenue Service provisions. Title II is applicable only to "tax-qualified plans" while Title I is much broader in coverage. It is applicable to both "tax-qualified" and "non-tax-qualified" plans. "Tax-qualified" in common usage would mean a plan for which the employer will obtain a current deduction for his contribution, while plan participants will not be taxed until benefits are distributed to them and earnings accumulate tax-free in a qualified pension trust.

28. ERISA § 3(3).

29. *Id.* § 3(1).

for periods extending to the termination of covered employment or beyond.³⁰ Any informal or formal program that defers income or provides for post-employment income must be closely scrutinized to see whether it falls within the confines of the definition.

In order to fall within the definition of an employee pension benefit plan, there must be a plan, fund or program. There need not exist a formal written plan embodied in a document; the plan may be an informal arrangement between the employer and employees. However, once the pension rights are classified as an employee pension benefit plan, they must be embodied in a written instrument.³¹ One commentator has expressed the opinion that a single deferred compensation agreement between an employer and an employee would fall within the confines of the definition, though he recognizes that the position could certainly be maintained that such an agreement does not constitute a "plan."³² But whether several similar agreements can be said not to constitute a plan is certainly open to question.

The plan, to be an employer pension benefit plan, must defer or provide retirement income for employees.³³ Thus, a plan for only self-employed individuals falls outside the scope of the definition since there are no employees.³⁴ Nor should an agreement with an independent contractor, in that the individual would not be classified as an employee. Furthermore, the plan must defer income to termination of employment or beyond.³⁵ Though no interpretive regulations have been issued on this point, it would appear that a plan, fund or program that defers income for a certain period of time, but which deferral would under no circumstances extend to termination of employment or beyond, is not within the Act's definition of a pension plan.³⁶

30. *Id.* § 3(2).

31. ERISA § 402(a)(1) requires that "[e]very employee benefit plan shall be established and maintained pursuant to a written instrument."

32. Sollee, *How the New Pension Reform Law Affects Non-Qualified Deferred Compensation Plans*, 41 J. TAXATION 324 (1974).

33. ERISA § 3(2).

34. *Id.* § 3(2); Instructions to IRS Form 5500-K (Nov. 1975).

35. ERISA § 3(2)(B).

36. A plan which would defer income for a definite time period but in which benefits would be payable to a participant only if he was in the active employ of the employer at the end of that time period would in all likelihood not fall within the definition.

ERISA exempts certain types of employee benefit plans from its coverage.³⁷ Generally, governmental plans, church plans, workmen's compensation plans, nonresident alien plans, and unfunded excess benefit plans are exempt from the Labor provisions of the Act. In addition, unfunded plans maintained by an employer primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees or agreements providing payments to retired or deceased partners, are exempt from most of the substantive provisions of Title I.³⁸ In order to come within the confines of the exemption a plan must be established primarily for highly compensated or managerial employees. No guidance is offered in the Committee Reports as to the meaning of "select group of management" or "highly compensated employees," terms that are not easily definable.³⁹ If the test is applied to a large corporation based on a cardinal salary criterion, it would encompass a large group. If, on the other hand, a percentage test were applied, say five or ten percent of the most highly compensated corporate employees, and if the corporation was small, in all likelihood the group would include a number of modestly paid employees. If a salary test were applied to a professional corporation, such as a law firm, the group of highly compensated employees would certainly include a great majority of the employees. Regulations will have to be published before any definitive answers can be given. Likewise, in order to come within the exception, the plan must be "unfunded." Again the Committee Reports offer no guidance in this area. The only guidance is previous Internal Revenue Service Rulings⁴⁰ shedding some light on the definition of "funded," but

37. ERISA § 4(b).

38. An exemption is provided under ERISA §§ 201(2), 301(a)(3), 401(a)(1) and 4021(b)(6). See Rustigan, *After the New Pension Law: Executive Compensation and Non-Qualified Plans*, 52 TAXES 896 (1974) [hereinafter cited as Rustigan]; Sollee, *How the New Pension Reform Law Affects Non-Qualified Deferred Compensation Plans*, 41 J. TAXATION 324 (1974).

39. Rustigan indicates that "highly compensated" is broader than "select group of management" in that this category should at least include all management personnel unless the corporation is arguably in such dire straits that one could say that its management personnel is poorly compensated. Rustigan at 899.

40. Rev. Rul. 72-25, 1972-1 CUM. BULL. 127; Rev. Rul. 68-99, 1968-1 CUM. BULL. 193; Rev. Rul. 55-525, 1955-2 CUM. BULL. 543.

there is no assurance that the Department of Labor will incorporate or adhere to them.⁴¹

Few plans, funds, or programs that provide employee fringe benefits in any manner, shape, or form will fall outside the definition of an employee welfare plan. Likewise, any plan, fund, or program deferring income is suspect of being an employee pension plan. The total exemptions from ERISA are few and closely defined, and the partial exemptions are fraught with danger and pitfalls.

DEFINITION OF A FIDUCIARY

A person is a "fiduciary" of an employee benefit plan to the extent:

(i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plans. Such term [also] includes any person designated . . . [by a named fiduciary to carry out fiduciary responsibility].⁴²

The definition first draws within its confines any person authorized to amend, alter, or terminate an employee benefit

41. It appears that the Department of Labor will take a strict approach to the definition of "unfunded," for a recently released regulation in its preamble indicates that any segregation of assets by the employer will make the plan funded, which goes beyond previous IRS rulings which apparently required the transfer of assets beyond the reach of the general corporate creditors in order to make the plan funded. Apparently the only safe course, until clarifying Department of Labor Regulations are promulgated in this area, would be to rely upon the pure naked promise of the employer. The promulgated regulation also indicates that any employee contributions will make the plan funded. Preamble, Dept. of Labor Regulation, § 2552.1 (December 19, 1974).

42. ERISA § 3(21)(A). A person is defined as an individual, partnership, joint venture, corporation, mutual company, joint stock company, trust, estate, unincorporated organization, association or employee organization. ERISA § 3(9). See Overbeck, *Persons upon Whom Duties and Obligations are Imposed Under the Employee Retirement Income Security Act of 1974*, 52 TAXES 881 (1974).

plan; thus, the employer, or plan sponsor,⁴³ is a fiduciary under the Act. Because a corporation acts through its board of directors, it is only natural to assume that board members will also be plan fiduciaries with respect to the plan.⁴⁴ A recent Interpretive Release by the Department of Labor indicates that board members are plan fiduciaries only to the extent they have responsibility for any of the functions described in the definition of fiduciary under § 3(21)(A).⁴⁵ The Release indicates that if the board of directors has the responsibility for the selection and retention of plan fiduciaries, board members would be deemed plan fiduciaries themselves, though their responsibility and consequently their potential liability would be limited to the selection or retention of plan fiduciaries. In all likelihood it is very difficult to exclude the board members as plan fiduciaries, in that their very position usually connotes great authority in dealing with the plan.

The second part of the fiduciary definition includes any person who exercises any authority or control respecting management or disposition of plan assets.⁴⁶ A plan trustee, presumed to have investment responsibility unless allocated to a "named fiduciary" or "qualified investment manager," will be a plan fiduciary.⁴⁷ If the investment responsibility has been delegated to a "qualified investment manager" or a named fiduciary, these persons will of course be plan fiduciaries.

43. See *Stafford*, FIDUCIARIES AND PARTIES-IN-INTEREST UNDER ERISA, at 68 (P.L.I. Tax Law and Practice Course Handbook Series No. 85); *Panel Discussion, Proceedings ABA National Institute, Fiduciary Responsibilities under the Pension Reform Act, May 30 and 31, 1975*, 31 THE BUSINESS LAWYER 85 (Special Issue 1975) [hereinafter cited as *Panel Discussion*].

44. For a complete discussion, see *Panel Discussion* at 86-98.

45. ERISA INTERP. BULL. 75-8, 29 C.F.R. § 2509.75-8 [hereinafter cited as INTERP. BULL. 75-8].

46. H. Conf. Rep. No. 93-1280, 93d Cong., 2d Sess., 74-3 U.S.C.C. & A.N. 5103 (1974) [hereinafter cited as H. Conf. Rep. No. 93-1280] states that "the substitute defines 'fiduciary' as any person who exercises any discretionary authority or control respecting management of a plan, exercises any authority or control respecting the management or disposition of its assets or has any discretionary authority or responsibility in the administration of the plan. Under this definition, fiduciaries include officers and directors of a plan, members of a plan's investment committee and persons who select these individuals. Consequently, the definition includes persons who have authority and responsibility with respect to the matter in question, regardless of their formal title."

47. ERISA §§ 402(a)(2), 3(38); H. Conf. Rep. No. 93-1280 at 5078-80.

A person is a plan fiduciary if he renders investment advice for a fee or other compensation or has the authority or responsibility to do so.⁴⁸ Proposed Regulations issued by the Department of Labor and the Internal Revenue Service provide that a person "renders advice to a plan" if he makes recommendations on purchasing or selling securities and if he has discretionary authority or control with respect to the investment of plan assets or provides advice to meet the particular investment needs of the plan and it is expected that such advice will serve as one of the primary bases for the investment of plan assets.⁴⁹ Apparently he need not render the advice for a fee in order to be a plan fiduciary. But the advice must be rendered on a regular basis with full knowledge that it will be used as the basis for the plan's investment decisions.⁵⁰

A person is a plan fiduciary if he has any discretionary authority or responsibility for the administration of the plan.⁵¹ Each plan must designate a "named fiduciary" who is charged with overall responsibility for the administration and operation of the plan.⁵² A "named fiduciary" is a fiduciary named in the plan instrument or, pursuant to a procedure specified in the plan, is identified as a fiduciary by a person who is an employer or by an employee organization.⁵³ The intent of this provision is to require the designation of some individual or some entity in order to enable plan participants, employees, or other interested parties to ascertain who is responsible for the operation and administration of the plan. The Department of Labor has taken the position that the named fiduciary must be designated in the instrument, either by name or by title.⁵⁴ There can, of course, be more than one named fiduciary, and any one person may be a named fiduciary with respect to a variety of plan responsibilities.

A "plan administrator" or "administrative committee" is normally the designation given to the named fiduciary charged with administrative responsibility. A person could

48. ERISA § 3(21)(A)(ii).

49. 26 C.F.R. § 54.4975-9.

50. *Id.*

51. ERISA § 3(21)(A)(iii).

52. *Id.* § 402(a)(1).

53. *Id.* § 402(a)(2).

54. ERISA INTERP. BULL. 75-5, 29 C.F.R. § 2509.75-5 [hereinafter cited as INTERP. BULL. 75-5].

become a fiduciary by accepting certain administrative plan responsibility pursuant to a proper designation by a named fiduciary. In order to become a plan fiduciary through the assumption of administrative responsibility, the person must assume discretionary authority. If the assumed responsibility is nondiscretionary and ministerial, merely carrying into effect policies, interpretations, rules, practices and procedures established by others, the person will not be a plan fiduciary.⁵⁵ In a similar vein, an attorney, accountant, actuary, or consultant who renders professional services other than investment advice does not become a plan fiduciary by virtue of his rendition. Advising plan fiduciaries or rendering services to the plan does not normally involve the exercise of any discretionary authority.⁵⁶

The distinction between a "fiduciary" and a "named fiduciary" is more than a matter of semantics. It can take on extreme importance not only in the administration of the plan but also in the accompanying responsibility and liability associated with that administration. Only named fiduciaries can allocate fiduciary responsibility among themselves and only named fiduciaries can designate other persons to carry out fiduciary responsibility.⁵⁷ Only certain named fiduciaries can appoint a qualified investment manager and only named fiduciaries can direct the trustee as to investment decisions.⁵⁸

BASIC FIDUCIARY RESPONSIBILITIES

A fiduciary is charged by ERISA with performing and carrying out his plan duties and responsibilities solely in the interest of the plan participants and their beneficiaries.⁵⁹ He must discharge his duties for the exclusive purpose of providing plan benefits and defraying reasonable expenses of ad-

55. INTERP. BULL. 75-8.

56. *Id.* 75-5.

57. If the plan specifically allows allocation or delegation and provides a procedure for it, named fiduciaries may allocate their specific responsibilities among themselves and named fiduciaries may delegate all or part of their duties (which do not involve asset management) to others. If such a proper allocation and delegation has been undertaken the fiduciary will not be liable for the acts or omissions of the persons to whom duties have been allocated or delegated. H. Conf. Rep. No. 93-1280 at 5081.

58. An investment manager can be appointed only by a named fiduciary charged with control or management of plan assets. ERISA § 402(c)(3).

59. ERISA § 404(a)(1).

ministration.⁶⁰ He must act with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in like capacity and familiar with such matters would use in conducting an enterprise of like character and with like aims.⁶¹ This statutory definition is more commonly referred to as the "prudent man rule." He must diversify investments so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so.⁶² He must act in accordance with the plan documents and instruments insofar as they are consistent with the provisions of ERISA.⁶³ A fiduciary may not, unless authorized by regulation, maintain plan assets outside the jurisdiction of the United States,⁶⁴ nor shall he engage in a "prohibited transaction."⁶⁵

Unfortunately, the Committee Reports shed very little light on the intended meaning and interpretation of the first of the enumerated fiduciary duties. The obvious import is that plan fiduciaries are to administer plans and discharge their duties with a view toward benefiting the plan participants and their beneficiaries and not the employer. Their actions must, at all times, be directed towards that goal.

The second fiduciary charge, the exclusive purpose test, originates from pre-ERISA Internal Revenue Service requirements.⁶⁶ The exclusive purpose test had been interpreted by the Internal Revenue Service broadly and would not appear to vary greatly from previous law.⁶⁷

The fiduciary standard that has received the greatest amount of notoriety and attention is the so-called "prudent man rule." The standard is a federal standard and varies from the traditional standard of fiduciary conduct in private trust law. The "prudent man rule" must be interpreted by taking into consideration the particular needs of employee benefit plans.⁶⁸ The rule, of course, applies to all plan

60. *Id.* § 404(a)(1)(A)(i),(ii).

61. *Id.* § 404(a)(1)(B).

62. *Id.* § 404(a)(1)(C).

63. *Id.* § 404(a)(1)(D).

64. *Id.* § 404(b).

65. *Id.* § 406(a)(1).

66. See H. Conf. Rep. No. 93-1280 at 5082; Mittelman, *The Exclusive Benefit Rule and Diversification*, 30 THE BUSINESS LAWYER 111 (1975).

67. *Id.*

68. H. Conf. Rep. No. 93-1280 at 5082; Klevan, *Fiduciary Responsibility*

fiduciaries, but it would have different applications depending on the fiduciary obligations that the fiduciary has assumed under the plan.

The applicability of the "prudent man rule" in the investment area has received the greatest amount of attention. The fiduciary charged with plan investment responsibility may be required to guarantee an investment rate of return, or the investment responsibility may be really nothing to worry about. The truth, as with most extremes, lies somewhere in between. Traditional private trust investment theories are not totally applicable in that most trustees are charged with carrying out the wishes and dictates of the settlor and generally have to consider both principal and income beneficiaries in any investment strategy. Clearly, there can be no one investment standard for all employee benefit plans, and the standard will vary with the particular plan needs and objectives.⁶⁹ The potential exposure for bad investments will also vary between different types of benefit plans. In a defined benefit pension plan, in which the employer bears the consequences of bad investments through the amortization of investment losses, the potential fiduciary liability for investments may not be great.⁷⁰ In an individual account plan, in which a participant's retirement benefits are directly affected by the rate of investment return, the fiduciary liability as to investments is greatly enhanced.⁷¹

A plan fiduciary is required to diversify plan assets, unless it is clearly prudent not to do so under the circumstances, in order to minimize the risk of large losses. If a potential claimant establishes that a plan fiduciary failed to diversify, the burden of proof shifts to the fiduciary to establish that it

Under ERISA's Prudent Man Rule: What Are the Guideposts?, 44 J. TAXATION 152 (1976) [hereinafter cited as Klevan]; Williams, *The Prudent Man Rule of the Pension Reform Act of 1974*, 31 THE BUSINESS LAWYER 99 (1975).

69. For excellent discussions of this area, see Comment, *Fiduciary Standards and The Prudent Man Rule under the Employee Retirement Income Security Act of 1974*, 88 HARV. L. REV. at 969-73 (1975); Klevan, *passim*.

70. ERISA § 3(35) defines a "defined benefit pension plan" in the negative by defining it as other than an individual account plan, defined by ERISA § 3(34). The employer is required to amortize bad investment losses under § 302(b)(2)(B) over a 15 year period, or 20 years for multi-employer plans.

71. The amount of retirement benefits available in an individual account plan are directly attributable to employer contribution and the rate of return on those contributions.

was prudent not to do so under the circumstances. The degree of investment concentration that would be in violation of this standard is difficult to measure, but the Committee Reports indicate that all facts and circumstances must be considered, including the purpose of the plan, the amount of plan assets, financial and industrial conditions, the type of investments, distribution as to geographic location, distribution as to industries, and dates of maturity.⁷² A fiduciary generally should not invest an unreasonably large proportion of the plan assets in a single security, one type of industry, or in a particular geographical location. Investment of all or substantially all of the plan assets in mutual funds, pooled investment funds, insurance, or annuity contracts will not violate the diversification requirements since these investment vehicles are presumed to have a great amount of diversification.⁷³

A fiduciary is required to carry out his responsibilities in accordance with the documents and instruments governing the plan, if they are not contrary to ERISA. Since ERISA requires that all employee benefit plans be maintained pursuant to a written instrument, the fiduciary does have guidance and would be advised to adhere to the written word unless it would contravene ERISA.

A fiduciary shall not cause the plan to engage in a "prohibited transaction" with a "party in interest"; if he does, he will be liable to the plan for its losses if he knows or should have known that the transaction was prohibited.⁷⁴ If a fiduciary enters into a "prohibited transaction" in his capacity other than as a fiduciary or enters into a transaction with himself, he will subject himself to certain Internal Revenue Service excise tax penalties.⁷⁵

72. H. Conf. Rep. No. 93-1280 at 5084-85.

73. *Id.* at 5085.

74. ERISA §§ 409(a), 406(a)(1). ERISA § 3(14) defines "[t]he term 'party-in-interest' . . . [as] (A) any fiduciary including, but not limited to, any administrator, officer, trustee, or custodian, counsel, or employer of such employee benefit plan; (B) the person providing services to such plan; (C) an employer any of whose employees who are covered by such plan; (D) an employee organization any of whose members are covered by such plan; (E) any owner, direct or indirect, of 50 percent or more of—(i) the combined voting power of all classes of stock entitled to vote or the total value of shares of all classes of stock of a corporation, (ii) the capital interest or the profits interest of a partnership, or (iii) the beneficial interest of a trust or unincorporated enterprise, which is an employer or employee organization described in subparagraph (C) or (D)"

75. The definition of a "disqualified person" is almost identical to "a

PROHIBITED TRANSACTIONS

A fiduciary who engages in a prohibited transaction will be personally liable for any plan losses or any profit made if he knew or should have known the transaction was prohibited.⁷⁶ The tax provisions of ERISA set forth almost identical transactions in which a "disqualified person" may not engage.⁷⁷ A fiduciary acting solely as a plan fiduciary, though coming within the definition of a "disqualified person," will not be subject to an excise tax on the prohibited transaction. But, if he engages in a transaction with the plan in other than his fiduciary capacity, he will be deemed to be a disqualified person and subject to the tax whether the transaction was undertaken with or without knowledge that it was prohibited.⁷⁸

The first prohibited transaction is a direct or indirect sale or exchange or a leasing of any property between a plan and a party-in-interest.⁷⁹ This provision also encompasses the transfer of property subject to a mortgage that the party-in-interest placed on the property within ten years from transfer in order that the rule on sales cannot be circumvented by

party-in-interest," though the prior is the correct terminology under the Internal Revenue Code, which defines it as a person who is "(A) a fiduciary; (B) a person providing services to the plan; (C) an employer any of whose employees are covered by the plan; (D) an employee organization any of whose members are covered by the plan; (E) an owner, direct or indirect, of 50 percent or more of—(i) the combined voting power of all classes of stock entitled to vote or the total value of shares of all classes of stock of a corporation, (ii) the capital interest or the profits interest of a partnership, or (iii) the beneficial interest of a trust or unincorporated enterprise, which is an employer or employee organization described in subparagraph (C) or (D)" INT. REV. CODE § 4975(e)(2). Although fiduciaries are disqualified persons under the tax provisions, they are to be subject to the excise tax only if they act in a prohibited transaction in a capacity other than that of a fiduciary. H. Conf. Rep. No. 93-1280 at 5101-02.

76. ERISA §§ 406(a)(1), 409(a); H. Conf. Rep. No. 93-1280 at 5087.

77. INT. REV. CODE OF 1954 § 4975(c)(1).

78. "Under the Labor provisions, a fiduciary will only be liable if he knew or should have known that he engaged in a prohibited transaction. Such a knowledge requirement is not included in the tax provisions. This distinction conforms to the distinction in present law in the private foundation provisions (where a foundation's manager generally is subject to a tax on self-dealing if he acted with knowledge, but a disqualified person is subject to tax without proof or knowledge)." H. Conf. Rep. No. 93-1280 at 5087.

79. ERISA § 406(a)(1)(A); H. Conf. Rep. No. 93-1280 at 5088. *See* GRAYCK, PROHIBITED TRANSACTIONS, FIDUCIARY RESPONSIBILITY AND PROHIBITED TRANSACTIONS UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT (P.L.I. Tax Law and Practice Course Handbooks Series No. 85).

placing an encumbrance on the property and then transferring it to the plan. Apparently this provision would not treat as a prohibited transaction an ordinary "blind purchase" of securities through an exchange if neither the buyer nor the seller knew the identity of the other party involved.

The second prohibited transaction is the direct or indirect extension of credit or the lending of money between a plan and a party-in-interest.⁸⁰ Apparently this far-reaching section would cover any transaction by which a party-in-interest would receive an indirect benefit through the use of plan assets. This provision may be somewhat troublesome in the area of "soft dollars" in the brokerage industry, where the employer, or a plan fiduciary, would have certain goods furnished to him upon having the requisite number of brokerage executions, even though those trades would be at best executions. Similarly, the funding of employer contributions with debt instruments will probably be prohibited in that a liability would exist between a party-in-interest and the plan. The guaranteeing of plan borrowings by a party-in-interest would constitute a prohibited transaction, unless it would come within the special exemption granted for employee stock ownership plans.⁸¹

The third prohibited transaction contained in both the labor and Internal Revenue provisions is the direct or indirect furnishing of goods or services or facilities between a plan and a party-in-interest.⁸² This provision also has far-reaching implications in that it appears to prevent a party-in-interest from deriving benefits from his relationship to the plan. The Committee Report indicates that the furnishing of personal living quarters to a party-in-interest is a prohibited transaction.⁸³

A fiduciary also may not directly or indirectly transfer any plan income or assets to or for the benefit of a party-in-interest.⁸⁴ The tax provisions use the wording "income or assets" while the labor provisions use only "assets," yet the legislative history establishes that both provisions should be interpreted in the same manner, and both apply to income and assets. The use of trust assets to manipulate the price of

80. ERISA § 406(a)(1)(B); H. Conf. Rep. No. 93-1280 at 5088.

81. *Id.* § 408(b)(3); H. Conf. Rep. No. 93-1280 at 5092-93.

82. *Id.* § 406(a)(1)(C); H. Conf. Rep. No. 93-1280 at 5089.

83. H. Conf. Rep. No. 93-1280 at 5089.

84. ERISA § 406(a)(1)(D); H. Conf. Rep. No. 93-1280 at 5089.

employer securities would constitute a prohibited transaction. This provision cannot always apply literally, since a lump-sum distribution to a terminating participant, considered a party-in-interest, would violate its technical language, but not its purpose.

A prohibited transaction found only in the labor provisions and not the tax provisions is the prohibition against the direct or indirect acquisition or holding by the plan of employer securities or real property.⁸⁵ But a plan may hold up to 10% of its plan assets in employer securities and employer real property.⁸⁶ A special exemption is provided for individual account plans, *i.e.*, profit sharing plans, stock bonus plans, employee stock ownership plans, thrift or savings plans, and certain money purchase plans. These individual account plans may exceed the 10% limit if the plan specifies the permissible amount of employer securities or qualifying real property that can be held by the plan.⁸⁷

The labor and tax provisions treat a fiduciary's dealing with the income or plan assets for his own interest or account as a prohibited transaction.⁸⁸ The receipt of consideration for the fiduciary's own personal account from any party dealing with the plan in connection with a transaction involving the income or assets of the plan constitutes a prohibited transaction. These provisions fall within the so-called "multiple services area."⁸⁹ Interestingly, neither of these provisions may apply to parties-in-interest or disqualified persons who are not fiduciaries.⁹⁰ They are designed to prevent inherent problems

85. *Id.* § 406(a)(1)(E); H. Conf. Rep. No. 93-1280 at 5089.

86. For the definition of "employer security," "employer real property," and "eligible individual account plan," see ERISA § 407(d).

87. For a complete discussion of these rules, see H. Conf. Rep. No. 93-1280 at 5097-98.

88. ERISA § 406(b)(1).

89. The phrase "multiple services" is not found in the statutory language of ERISA but is discussed in the Committee report as a shorthand expression in describing those situations in which a person acts on behalf of a plan in several capacities.

90. H. Conf. Rep. No. 93-1280 at 5095 provides "[u]nless otherwise specifically allowed by statutory or administrative exemption, generally a fiduciary is not to be able to provide 'multiple services' to a plan. *However, the prohibition against providing multiple services is not to apply to parties-in-interest, who are not fiduciaries.* This rule was adopted because of the potential problems inherent in situations where persons who can act on behalf of a plan also are in a position to personally benefit at the expense of

when a person acts in a dual relationship to the plan and thus is in a position personally to benefit at the expense of the plan in carrying out his responsibility. In view of the fact that these rules may not be applicable to fiduciaries, the definition of fiduciary is a critical determination in the multiple service area.

The multiple service problem is especially acute in the insurance industry since a pension consultant may receive a commission on the sale of insurance used to fund benefits under the plan, and if the consultant is a plan fiduciary, the commissions would violate the multiple service rules. On the other hand, if he is not a plan fiduciary, but a party-in-interest or a disqualified person, he could apparently provide multiple services to the plan without violating the prohibited transaction rules. Stockbrokers who provide investment management services to a plan and at the same time furnish brokerage services on a transaction which they direct encounter a similar problem.⁹¹ The structure obviously presents an opportunity for churning of assets. If the stockbroker is a plan fiduciary, he violates the multiple services rule. Broker-dealers, reporting dealers, and banks benefit from an interim exemption as to certain transactions that would otherwise be prohibited.⁹²

The labor provisions of ERISA, though not the tax provisions, prohibit a fiduciary from acting in any transaction involving the plan on behalf of a person, or representing a party with adverse interest to those of the plan or its participants. The import of this provision is to prevent a plan fiduciary from being placed in a position where he would have dual loyalties and allegiances.⁹³

EXEMPTION FROM PROHIBITED TRANSACTIONS

The exemptions from the prohibited transaction rules are divided into two main parts. The first part, a general dis-

the plan in exercising that authority" (emphasis added). Though this is specifically set forth in the Conference Committee Report, it has been seriously questioned. See Neal & Brett, *ERISA Limitations on the Performance of "Multiple Services" by Fiduciaries*, 44 J. TAXATION 90 (1976).

91. H. Conf. Rep. No. 93-1280 at 5089-90.

92. See Proposed Exemptions from Prohibitions Respecting Certain Classes of Transactions Involving Employee Benefit Plans and Certain Broker-Dealers, Reporting Dealers and Banks, 40 Fed. Reg. No. 152 (August 6, 1975).

93. H. Conf. Rep. No. 93-1280 at 5089.

cretionary procedure, requires the Secretary of Labor and the Internal Revenue Service, respectively, to establish an exemption procedure pursuant to which an exemption from any of the prohibited transaction provisions can be sought. The determination is to be a joint effort and the exemption should be granted only if the respective departments find that it is administratively feasible, is within the interest of plan participants and their beneficiaries, and protects the rights of participants and their beneficiaries.⁹⁴ The area of major activity has been in the investment area. There, the Department of Labor and the Internal Revenue Service have granted certain interim exemptions.⁹⁵

In addition, some transactions are generally exempt from the prohibited transactions rules. For instance, the plan may provide for loans to plan participants or their beneficiaries under certain circumstances.⁹⁶ The loans must be in accord with specific plan provisions, and they must carry a reasonable rate of interest and be adequately secured. They must be made available to all plan participants on a nondiscriminatory basis except as to credit-worthiness.⁹⁷ A party-in-interest or a disqualified person may also furnish to a plan office space, legal services, accounting services or other similar services necessary for the establishment or operation of a benefit plan, if no more than reasonable compensation is paid for these services.⁹⁸ The arrangements cannot be on a long-term basis and must provide for termination on a reasonably short notice, so that the plan will not be locked into a disadvantageous long-term arrangement. Also, the plan may pay a fiduciary or other party-in-interest reasonable compensation for services rendered to the plan if the services are reasonably necessary but only if the fiduciary or party-in-interest is not receiving full-time pay from the employer or the sponsoring association. It is permissible for the plan to reimburse expenses properly and actually incurred by the fiduciary and not otherwise reimbursed.⁹⁹

Certain loans made to an employee stock ownership plan

94. ERISA § 408(a); INT. REV. CODE § 4975(c)(2); H. Conf. Rep. No. 93-1280 at 5091.

95. Prohibited Transaction Exemption 75-1, Dep't of Labor, IRS, 29 C.F.R. § 2509.75-10.

96. ERISA § 408(b)(1); H. Conf. Rep. No. 93-1280 at 5092.

97. *Id.*

98. ERISA § 408(b)(2); H. Conf. Rep. No. 93-1280 at 5092.

99. *Id.*

(ESOP) are exempt.¹⁰⁰ This exemption is necessary in order to legitimate the common practice of these plans to purchase an employer's stock from major shareholders or from the employer itself; the proceeds to buy the stock are often obtained from an unrelated lender with a guarantee of repayment by the employer. Also, it is common practice for the shareholder selling his stock to the ESOP to take back a note. Since often the selling shareholder is a party-in-interest, such a transaction, but for the exemption, would constitute a prohibited transaction. This exception is available only to employee stock ownership plans and not to other types of employee benefit plans.¹⁰¹

A bank or similar institution that is a plan fiduciary may invest all or part of the plan assets in deposits with itself, if those deposits bear a reasonable rate of interest and if the plan covers only employees of the institution or if such investment is specifically authorized by a plan fiduciary (other than the institution) or by the plan instrument itself.¹⁰²

In addition the plan may purchase life insurance, health insurance or annuities from the employer maintaining the plan, if the employer is an insurance company qualified to do business in a state or the District of Columbia.¹⁰³ The plan may not pay more than adequate consideration for the insurance.

Generally, a fiduciary is not able to provide multiple services to a plan, but an exemption is provided for banks or similar financial institutions that are supervised by the federal or state authorities under certain circumstances.¹⁰⁴ First, the bank can charge no more than a reasonable rate of compensation. It must establish adequate internal safeguards to assure that its provision of ancillary services is in accord with sound banking and financial practices, as determined by federal and state banking authorities. The services must be provided in accordance with binding, specific

100. ERISA § 408(b)(3); H. Conf. Rep. No. 93-1280 at 5092-93. See the H. Conf. Rep. No. 93-1280 at 5093 for a discussion as to the anticipated parameters of an employee stock ownership plan; see also Hoggert, *Employee Stock Ownership Trusts*, 53 TAXES 305 (1975); Kaplan, *Esop's Fable*, 53 TAXES 898 (1975).

101. ERISA § 408(b)(3); H. Conf. Rep. No. 93-1280 at 5093.

102. *Id.* § 408(b)(4); H. Conf. Rep. No. 93-1280 at 5094.

103. *Id.* § 408(b)(5); H. Conf. Rep. No. 93-1280 at 5094.

104. *Id.* § 408(b)(6); H. Conf. Rep. No. 93-1280 at 5095.

guidelines that will prevent the bank from providing ancillary services in an unreasonable or excessive manner or that would violate the best interests of the plan participants or their beneficiaries.

Certain employee benefit plans may hold or acquire employer securities. Since some of these securities may be convertible, bonds to stocks, a conversion is not a prohibited transaction if the plan receives at least fair market value under the conversion.¹⁰⁵ Of course, the conversion must be reasonable under the circumstances, and in keeping with the interest of the plan participants and their beneficiaries.

Banks, trust companies, and insurance companies may maintain pooled investment funds for plans.¹⁰⁶ In order to come within this exception, the plan instrument or a plan fiduciary who has the authority to manage and control the plan assets must specifically authorize the investment of plan assets in the fiduciary's own sponsored pooled investment fund.¹⁰⁷

Finally, an overriding exemption is provided for the distribution of plan assets in accordance with the applicable rules of ERISA or in accordance with the terms of the plan instrument.¹⁰⁸

CIVIL LIABILITY

Under the labor provisions of ERISA, any fiduciary who breaches his fiduciary responsibility will be personally liable for any losses to the plan resulting from the breach and for restoring to the plan any profits he may have made through the breach.¹⁰⁹ The tax provisions impose nondeductible excise taxes on disqualified persons but not on fiduciaries unless acting in a capacity other than that of a fiduciary, for entering into certain prohibited transactions.¹¹⁰ There are, of course, many specific penalties imposed upon a plan fiduciary for failing to carry out certain mandatory administrative plan responsibilities.

Generally, while a fiduciary is not liable for any breach of

105. *Id.* § 408(b)(7); H. Conf. Rep. No. 93-1280 at 5095-96.

106. *Id.* § 408(b)(8); H. Conf. Rep. No. 93-1280 at 5096.

107. *Id.* § 408(b)(8); H. Conf. Rep. No. 93-1280 at 5096.

108. *Id.* § 408(b)(9); H. Conf. Rep. No. 93-1280 at 5097.

109. *Id.* § 409(a).

110. See notes 74-75, *supra*.

fiduciary responsibility that occurred before he became a plan fiduciary or after he no longer holds such a plan position,¹¹¹ he is subject to appropriate actions that may be brought against him, including his removal from a fiduciary position. Plan participants, beneficiaries, or the Department of Labor may enforce his duties.¹¹² An action to enforce a breach of fiduciary responsibility or an action to enforce or clarify benefit rights under the labor provisions lies exclusively in the United States district courts. Suits to enforce benefit rights or to recover benefits under the plan that do not involve application of the labor provisions of ERISA may be brought not only in the federal district courts but also in state courts of competent jurisdiction. Jurisdiction, if appropriate, lies in federal district courts without regard to the amount in controversy or citizenship of the parties.

In any court action, the court may allow reasonable attorney's fees or other costs to either party. If a participant or a beneficiary initiates an action in a federal district court to enforce his rights under the labor provisions of ERISA, he must provide a copy of the complaint to the Secretaries of Labor and Treasury.¹¹³ A copy of the complaint is not required in an action solely for the purpose of recovering benefits under the plan. The Secretaries of Labor and Treasury both may intervene in any action at their discretion.¹¹⁴

In addition to the numerous redresses available to private litigants and the ability of the Secretaries of Labor and Treasury to intervene, the Act authorizes the Secretary of Labor to seek an injunction for breach of fiduciary duty to enjoin any action or practice by a plan fiduciary that violates the labor provisions or to obtain other appropriate relief or to enforce any provision of the labor provisions of ERISA. In addition, the Secretary of Labor may assess upon a party-in-interest civil penalties, analogous to the excise tax penalties found under the tax provisions, with respect to the non-tax-qualified plans where there has been a prohibited transaction.¹¹⁵

111. ERISA § 409(b).

112. See ERISA § 502; H. Conf. Rep. No. 93-1280 at 5106-07.

113. A suit to enforce benefit rights under a plan that does not involve the labor provisions of ERISA may be brought in a state court of competent jurisdiction. ERISA § 502(e)(1).

114. *Id.* § 502(h).

115. *Id.* § 502(i).

The Secretary of Labor has broad authority and power to investigate potential violations of fiduciary duties. He can request the submission of reports, books and records but he cannot request them more than once a year. He is given subpoena powers identical to those available to the Federal Trade Commission in order to enforce his investigatory role.¹¹⁶

Generally, no action may be commenced under the labor provisions as to a breach of fiduciary's responsibility, duty or obligation after the earlier of six years after the date of the last action which constituted a part of such breach or violation or, in the case of an omission, the latest date in which the fiduciary could have cured the breach or violation, or three years after the earliest date on which the plaintiff had actual knowledge of the breach or violation or in which a report from which he could have reasonably expected to have obtained such knowledge of such breach or violation was filed with the Secretary of Labor.

CO-FIDUCIARY LIABILITY

A plan fiduciary is personally liable for any loss caused by a breach of fiduciary responsibility by another fiduciary under certain specified circumstances. If a fiduciary knowingly participates in or knowingly undertakes to conceal an act or omission of a co-fiduciary which he knows constitutes a breach, liability will be imposed upon him.¹¹⁷ If *A* and *B* are co-trustees and the terms of the trust provide that they are not to invest in commodity futures, and *A* suggests to *B* that *B* invest part of the plan assets in commodity futures, if *B* does so, *A*, as well as *B*, is liable for the breach. If a plan fiduciary knowingly conceals a breach of fiduciary obligation committed by another plan fiduciary, he will be liable. Assume *A* and *B* are co-trustees, and *B* invests in commodity futures in violation of the trust instrument. If *B* tells his co-trustee *A* of this investment, *A* would be liable with *B* for breach of fiduciary responsibility if he conceals this investment.¹¹⁸

A fiduciary is also liable if he knows that another

116. See *id.* § 504.

117. *Id.* § 405(a)(1).

118. H. Conf. Rep. No. 93-1280 at 5080.

fiduciary of the plan has committed a breach and he does not take reasonable steps under the circumstances to remedy it.¹¹⁹ In the above examples the fiduciary gaining knowledge of the breach of responsibility by the co-fiduciary may be required to dispose of the commodity futures if he has the authority to do so and if it would be prudent under the circumstances. Alternatively, the appropriate step may be to notify the plan sponsor of the breach, to proceed in the appropriate federal court for instruction or to bring the matter to the attention of the Secretary of Labor. The proper remedy required under the facts and circumstances will vary, of course, with each individual case, but apparently the fiduciary must take some form of affirmative action to attempt to remedy the breach to avoid liability.¹²⁰

A fiduciary is liable for the loss caused to the plan by the breach of fiduciary responsibility of another fiduciary if he has enabled the other fiduciary to commit a breach through his failure to exercise prudence or to comply with the basic fiduciary rules of the labor provisions in carrying out his specific responsibility.¹²¹ If *A* and *B* are co-trustees to jointly manage the plan assets, and if *A* improperly allows *B* to have sole custody of the plan assets and makes no inquiry as to his conduct, while *B* is thereby enabled to sell the property and to embezzle the proceeds, *A* is liable for a breach of fiduciary responsibility.¹²²

ALLOCATION OF FIDUCIARY RESPONSIBILITY

ERISA clearly allows plan fiduciaries to allocate fiduciary responsibility among themselves. The plan must specifically allow allocation or delegation and must expressly provide a procedure for it.¹²³ A proper allocation or delegation of responsibility also allocates or delegates the fiduciary liability; of course, the co-fiduciary liability rules still apply.¹²⁴

If plan assets are held by one trustee, it is assumed that the trustee has sole and absolute authority to manage and control the plan assets unless the authority has been dele-

119. ERISA § 405(a)(2).

120. *Id.*; H. Conf. Rep. No. 93-1280 at 5085-86.

121. ERISA § 405(a)(3).

122. H. Conf. Rep. No. 93-1280 at 5080.

123. ERISA § 402(b)(2).

124. *Id.* § 405(c)(1); H. Conf. Rep. No. 93-1280 at 5081-82.

gated or allocated to a named plan fiduciary or to a qualified investment manager. If the plan provides for two or more trustees, they jointly have the responsibility for the management and control of plan assets,¹²⁵ but the trust instrument can provide for an allocation and delegation of trust responsibility among various trustees. If so, a trustee will not be liable for any losses that arise from acts or omissions of the co-trustee to whom the responsibilities have been allocated. Though a trustee is not liable for the actions of a co-trustee under these circumstances, a co-trustee will be liable notwithstanding if he fails to comply with other applicable fiduciary standards.¹²⁶ If plan assets are held in separate trusts, the trustee of one trust is not responsible as a co-trustee of another trust.

Though it is presumed that a trustee will have investment authority with respect to plan assets, it is possible to structure the plan instruments so that the trustee will be subject to the proper direction of a named fiduciary who is not a trustee. The plan instrument must specifically provide for this and the trustee will, under such a structure, subject himself to potential co-fiduciary liability for investment decisions.¹²⁷

In addition, the plan may permit individual participants to exercise independent control over the investment of plan assets in their own individual accounts.¹²⁸ If so, they are not plan fiduciaries, and plan fiduciaries will not be liable for any investment loss resulting from the directed investment decisions of the plan participants.¹²⁹

DELEGATION OF INVESTMENT RESPONSIBILITY

The major area of potential liability under ERISA accompanies investment responsibility for plan assets. A plan fiduciary charged with investment responsibility is not in any manner guaranteeing an investment rate of return, though he should not treat his responsibility with a cavalier attitude. He will be held to a certain conduct of prudence judged by

125. *Id.* § 405(b)(1); H. Conf. Rep. No. 93-1280 at 5080.

126. H. Conf. Rep. No. 93-1280 at 5081.

127. The trustee will be subject to the co-fiduciary provisions of ERISA § 405(a).

128. ERISA § 404(c).

129. *Id.*; H. Conf. Rep. No. 93-1280 at 5085-86.

varying degrees, depending on the expertise he professes to have. In view of these potentially onerous provisions, much attention should be given to the proper allocation of investment responsibility among plan fiduciaries and the structuring of the plan instrument in such a way as to clearly delegate and isolate this potential liability.

A named fiduciary with respect to the control and management of plan assets may appoint a qualified investment manager to manage all or part of the plan assets, but there is some confusion under the Act whether a plan trustee is a "named fiduciary" and thus able to appoint a qualified investment manager. The named fiduciary, in choosing and retaining an investment manager, does have fiduciary responsibility to oversee his performance. If he appoints a qualified investment manager, he no longer has responsibility for managing the assets controlled by the qualified investment manager and would, generally, not be liable for the acts or omissions of the investment manager. He would only be liable if he knowingly participated in or knowingly undertook to conceal an act or omission by the investment manager that he knew constituted a breach of fiduciary responsibility.¹³⁰ In contrast, if a trustee is subject to the direction of a named fiduciary as to investment decisions, his co-fiduciary liability would be more extensive.¹³¹

If plan assets are held in one or more separate trusts or distinct portions of one trust, each trustee is charged only with investment responsibility and potential liability as to plan assets contained in that trust. The potential liability here is closely akin to the appointment of a qualified investment manager. If, on the other hand, one trust instrument is used with several co-trustees, even though the instrument specifically provides for the allocation of trust responsibilities among the co-trustees, a trustee is subject to the general co-fiduciary liability provisions of ERISA.¹³²

130. ERISA § 405(d)(1). This section would limit co-fiduciary liability to § 405(a)(1).

131. Under this structure all of the co-fiduciary liability provisions of § 405(a) are applicable. The trustee is relieved of liability under § 403(a)(1) upon following "proper directions of such fiduciary which are made in accordance with the terms of the plan and which are not contrary to this title . . ." In view of this distinction, it generally is not advisable for banks to assume the position of trustee and be subject to directed investments by a named fiduciary.

132. H. Conf. Rep. No. 93-1280 at 5081.

If a plan provides for individual accounts and permits the plan participants to make their own investment decisions and such decisions are exercised truly on an independent basis, little or no potential investment liability exists. If a plan instrument provides that the trustee is subject to the direction of a named fiduciary as to investment decisions, the trustee is not liable for following his proper directions made in accordance with the terms of the plan and consistent with the labor provisions of ERISA. Under this structure, the trustee has more exposure under the co-fiduciary liability provisions in that he is subject to ascertaining whether the decisions by the named fiduciary are made in accordance with the terms of the plan and are not contrary to the provisions of ERISA. If a trustee is charged with investment responsibility and retains an investment advisor, differentiating between an investment advisor and a qualified investment manager, the trustee has not relieved himself of investment liability and the investment manager will probably be deemed a plan fiduciary.

As can be seen from the above, a great variety of structures can be undertaken, some shifting and obligating investment responsibility and potential liability, others only adding additional plan fiduciaries to that responsibility and liability. It is imperative to understand that various structures will have varying degrees of protection in absolving a fiduciary of potential fiduciary liability.

MISCELLANEOUS PROVISIONS

Exculpatory Provisions

Any exculpatory language that attempts to relieve a fiduciary from liability for breach of his responsibility is void.¹³³ Though exculpatory clauses are invalid, the Department of Labor has recognized the validity of indemnification agreements given to a plan fiduciary by an employer or a plan sponsor.¹³⁴ A plan may also purchase insurance to protect itself against any loss resulting out of a breach of fiduciary responsibility, although the insurance purchased by the plan

133. ERISA § 410(a).

134. ERISA INTERP. BULL. 75-4 (June 4, 1975), 29 C.F.R. § 2509.75-4.

must allow recourse by the insurer against the fiduciary.¹³⁵ A fiduciary can also purchase insurance to protect himself against potential liability arising out of a breach of his fiduciary duties or his employer can purchase such for him.¹³⁶ The Department of Labor has issued an Interpretative Bulletin validating a common practice by which a plan takes out insurance and part of the insurance policy is a waiver of recourse by the insurer as against the plan fiduciary, but the premium for the waiver of recourse must be paid by the plan fiduciary.¹³⁷

Bonding Provisions

Every plan fiduciary, and other persons who handle funds or fund property, jointly called plan officials, must be bonded.¹³⁸ This provision is identical to an analogous provision in the Welfare and Pension Plan Disclosure Act,¹³⁹ and Congress intended that it be given a similar interpretation.¹⁴⁰ A bond is not required if plan benefits are paid solely from the assets of the employer or union nor is it required of a domestic trust or insurance corporation subject to federal supervision or examination, if the trust or corporation has capital and surplus in excess of \$1 million.

Prohibition Against Certain Persons Holding Offices

Persons who have been convicted of certain specified crimes may not serve as plan administrators, fiduciaries, officers, trustees, custodian counsel, agents, employees or consultants of the plan for five years after conviction or five years after the end of imprisonment, whichever is later.¹⁴¹ Such a person may serve in any one of the above capacities if his citizenship rights have been fully restored or if the United States Board of Parole determines that his services would not be contrary to the purposes of the labor provisions of ERISA. Rather stringent penalties are provided for violating this sec-

135. ERISA § 410(b)(1).

136. *Id.* § 410(b)(2), (3).

137. Dept. of Labor News Release (Mar. 4, 1975).

138. ERISA § 412; H. Conf. Rep. No. 93-1280 at 5104.

139. H. Conf. Rep. No. 93-1280 at 5104.

140. *Id.*

141. ERISA § 411; H. Conf. Rep. No. 93-1280 at 5104.

tion; those who intentionally violate the provision may be fined up to \$10,000 and imprisoned for up to one year.

CONCLUSION

ERISA is having and will continue to have a major impact on employee benefit plans. The fiduciary provisions of the Act will in their fullest measure only be felt, understood, hated or appreciated with the passage of time.

